



**BB&T Corporation**

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July 13, 2018

**Daryl Bible**  
Chief Financial Officer

Ms. Ann E. Misback  
Secretary  
Board of Governors of the Federal Reserve System  
20th Street and Constitution Avenue NW,  
Washington, DC 20551

Re: Docket No. R-1605 and RIN 7100-AF 04

Dear Ms. Misback:

Branch Banking and Trust Company and subsidiaries of BB&T Corporation (collectively referred to as “BB&T”) appreciate the opportunity to comment on the notice of proposed rulemaking (“Proposal”) that would implement the current expected credit loss (“CECL”) methodology into the regulatory capital rules<sup>1</sup> (collectively, the “capital rules”) of the Office of the Comptroller of the Currency, Board of Governors of the Federal Reserve System and the Federal Deposit Insurance Corporation (collectively, the “Agencies”), as published by the Agencies on May 14, 2018. Please accept this letter as BB&T’s position regarding the Proposal.

BB&T Corporation (NYSE: “BBT”) is one of the largest financial services holding companies in the U.S., with \$220.7 billion in assets and a market capitalization of approximately \$40.6 billion as of March 31, 2018. Building on a long tradition of excellence in community banking, BB&T offers a wide range of financial services including retail and commercial banking, investments, insurance, wealth management, asset management, mortgage, corporate banking, capital markets and specialized lending. Based in Winston-Salem, N.C., BB&T operates more than 2,000 financial centers in 15 states and Washington, D.C. A Fortune 500 company, BB&T is consistently recognized for outstanding client service by Greenwich Associates for small business and middle market banking. More information about BB&T and its full line of products and services is available at [BBT.com](http://BBT.com).

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<sup>1</sup> 12 C.F.R. Part 217 (Board) and 12 C.F.R. Part 324 (FDIC). The Proposal will amend the Capital Rules to reflect the changes to U.S. GAAP resulting from FASB’s issuance of ASU No. 2016-13, Financial Instruments – Credit Losses as it relates to the calculation of regulatory capital ratios.

### **Executive Summary**

CECL represents the most consequential change to accounting rules impacting financial institutions in recent history. BB&T actively engaged with the Financial Accounting Standards Board (“FASB”), the Agencies and the United States Securities and Exchange Commission (“SEC”) throughout the standard-setting process, and has previously provided feedback that outlined our primary concerns related to the standard’s impact on financial institutions, financial statement users and perhaps most importantly, consumers and businesses in the United States. These concerns include the following:

- CECL is inconsistent with the economics of lending, and therefore will not provide financial statement users with decision-useful information.
- The pro-cyclicality of CECL will exacerbate economic cycles, which will have a significant impact on consumers and businesses.
- CECL will likely drive unintended changes to the price, availability and structure of credit in the United States.
- Financial statement comparability will be challenged by the interpretation and application of the principles-based standard.
- U.S. banks will be placed at a competitive disadvantage, as International Financial Reporting Standards 9 requires life-of-loan loss estimates on a much smaller portion of the portfolio compared to CECL.
- CECL will drive effective capitalization to unnecessarily high levels.

In preparing this response to the Proposal, BB&T concluded that it was appropriate to include certain recommendations that are not necessarily within the control of the Agencies. Specifically, we believe that CECL has not been appropriately evaluated through the lens of its potential impact to the price, availability and structure of credit, nor the potential for other long-term economic and systemic impacts to the overall economy. Accordingly, BB&T is recommending that the Agencies actively engage with the FASB to seek a delay in the implementation of CECL to provide appropriate time for such a study to be completed.

BB&T also believes that it would be prudent for the Agencies to evaluate modifications to CECL that strike a more appropriate balance between the needs of all stakeholders. We have put forth one such recommended approach in this letter, which we believe provides financial statement users with decision-useful information related to expected credit losses, while at the same time ensuring that the resulting financial reporting faithfully depicts the economics of lending transactions. We acknowledge that this recommendation requires additional analysis and evaluation, but are committed to working with other financial institutions, the Agencies and the FASB to demonstrate how this recommendation represents a viable alternative to CECL.

Regardless of the outcome of efforts to modify CECL, BB&T believes the Agencies must move in the direction of providing capital relief in connection with the adoption of CECL. In a letter to Representatives Zeldin and Budd, FASB stated, “Regulatory capital requirements and other public policy considerations are decisions appropriately left to regulatory and legislative bodies.”<sup>2</sup> The current regulatory capital framework was designed in contemplation of the existing incurred loss methodology used to record credit losses. Current minimum capital requirements reflect consideration of both expected credit losses (i.e., expected losses that have not yet been incurred and included in the allowance for credit losses) as well as unexpected credit losses. As a result, the adoption of CECL (or a modified version of CECL) would result in an increase to effective capitalization levels absent a change to the current minimum capital requirements, since expected credit losses will be fully provided for in the allowance for credit losses, and will also be inherently considered in regulatory capital requirements. Adjustments to the regulatory framework, whether through regulatory capital adjustments (e.g., an adjustment to the CET1 capital calculation) or changes to minimum capital requirements, must be considered.

Finally, we have provided feedback related to the incorporation of CECL into the stress testing process. The incorporation of CECL into the stress testing process must strike an appropriate balance between operational simplicity, transparency and the avoidance of unintended consequences. The complexity of the CECL estimation process does not lend itself well to requiring a full CECL estimate for each quarter of the forecast horizon. As a result, BB&T recommends the Agencies continue to provide financial institutions with the flexibility to use practical expedients such as coverage ratios, in forecasting changes to CECL estimates over the nine quarter period.

These recommendations have been described in further detail in the remainder of this letter.

### **Macro-Economic Evaluation of CECL Must be Performed**

CECL fundamentally changes how companies will recognize credit losses in their loan and held-to-maturity debt security portfolios by requiring upfront recognition of credit losses that are expected over the contractual life of the asset. While modeling efforts associated with the implementation of CECL are ongoing, preliminary results have indicated that longer-tenor consumer portfolios will generally require higher CECL reserves, while reserves related to commercial lending products will generally decrease when compared to the existing incurred loss approach. These results reflect the nature of commercial lending compared to consumer lending (i.e., commercial lending agreements typically reflect shorter terms that provide lenders with the opportunity to re-underwrite the loan in connection with a renewal, whereas consumer loans typically reflect longer terms).

BB&T believes that CECL effectively establishes incentives (or in some cases, disincentives) that will drive future lending decision-making. These incentives could have significant impacts to residential mortgage lending, based on their longer contractual terms, and small business and subprime lending, based on the higher levels of expected credit losses inherent in these types of lending. Further, these incentives will be magnified in periods of economic stress, as financial institutions attempt to avoid growth in loan portfolios with immediate negative impacts to capital.

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<sup>2</sup> FASB letter to Representatives Zeldin and Budd, dated November 3, 2017.

As these issues and others have both macroeconomic and public policy implications, and in light of the U.S. Treasury Department report<sup>3</sup> that “promotes a more robust banking system,” it is imperative that an evaluation of the standard’s effect on the overall stability of the banking sector and on the availability, accessibility and affordability of credit be performed to avoid unintended consequences. Such a study would likely require input from financial institutions, the Agencies, FASB and other stakeholders, and a result would likely represent a time-consuming process. Further, it would be critically important to identify an organization that could conduct such a study with an appropriate degree of impartiality and objectivity. With CECL’s required implementation date quickly approaching, BB&T believes that a delay in full implementation is necessary to provide time to conduct such a study and appropriately address any negative consequences identified therein.

### **Modifications to CECL Warrant the Agencies’ Attention**

Notwithstanding the need for an evaluation as described above, BB&T also believes that it would be prudent for the regulators to consider modifications or adjustments to the CECL model. While any potential changes to CECL must be promulgated by the FASB, the Agencies are in a unique position to advocate for changes that more appropriately balance the needs of financial statement users, financial institutions and the regulatory agencies. One potential adjustment to the CECL model that has merit is described as follows:

- Maintain a CECL-compliant allowance for credit losses<sup>4</sup> (“ACL”) estimate on the balance sheet.
- The ACL estimate would be composed of two components; an estimate of expected losses over the next twelve months, and an estimate of credit losses over the remainder of the contractual term of the underlying financial instruments.
- Subsequent changes to the ACL would be recorded as follows:
  - Expected losses over the next twelve months – would be reflected as a component of the provision for credit losses in the income statement;
  - Expected losses over the remainder of the contractual term – would be reflected in other comprehensive income.

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<sup>3</sup> U.S. Department of the Treasury. (June 2017) “A Financial System That Creates Economic Opportunities – Banks and Credit Unions” p.50

<sup>4</sup> For the purposes of this letter, Allowances for Credit Losses (“ACL”) refers to allowance for loan and lease losses plus the reserve for unfunded commitments, which are eligible for inclusion in capital. Under the Proposal, the definition of ACL and the amount includable in capital will change slightly due to the implementation of CECL.

BB&T believes that such an approach would provide financial statement users with decision-useful information related to expected credit losses, and ensure that the income statement recognition of credit losses is appropriately linked to the underlying economics of lending transactions. Additional benefits associated with such an approach include the following:

- Mitigation of financial institutions' concerns regarding the inherent loan growth disincentive in CECL, as life-of-loan credit loss estimates would no longer flow directly to the income statement (and therefore capital) in connection with loan portfolio growth.
- Opportunity to achieve a greater degree of convergence with international accounting standards, which initially represented a significant area of focus for the FASB.
- Consistent with FASB's CECL accounting objectives of presenting financial assets at the amount expected to be collected over the life of the asset.
- Maintains the ability to consider forecasts of economic conditions in connection with the allowance estimation process, which provides financial institutions with the flexibility to build reserves earlier than the current incurred loss model.

#### **Permanent Changes to the Regulatory Capital Framework Must Be Adopted**

While the proposed modifications to CECL described above provide relief from a financial reporting perspective, BB&T continues to believe that permanent adjustments to the regulatory capital framework will be required in connection with the adoption of CECL (or any modified version of CECL that changes the nature of the credit loss recognition process). The implementation of an expected credit loss approach (whether fully recognized in the income statement or partially recognized in accumulated other comprehensive income) has significant implications from a capital perspective, as capital that was previously required to provide for expected losses that had not yet been incurred, would no longer be required as such amounts would either be reflected in retained earnings or accumulated other comprehensive income.

The current minimum capital requirements were designed to ensure banks have sufficient capital to sustain operations in stress, considering risk profile and levels of credit risk. CCAR and the proposed Stress Capital Buffer ("SCB") already consider the capital required to sustain operations in stress when setting the minimum capital requirements for large banking organizations. The Proposal does not change minimum capital requirements or address how CECL will be incorporated into CCAR or the SCB. The Proposal will result in banks recognizing future credit risk into capital levels (due to CECL) and simultaneously holding more capital for sustaining operations in stressful credit conditions (due to the SCB), effectively double counting future credit risk in both capital level and minimum capital requirements.

The Agencies' Proposal provides for a transition adjustment over the three years following the adoption of CECL. BB&T does not believe that such provisions provide meaningful capital relief as financial institutions will immediately make capital allocation decisions based upon the long-term impact of CECL and the proposed transition relief will not preempt such decisions.

Additionally, such transition adjustments are generally disregarded by the financial markets, as greater focus is typically given to capital ratios calculated on a fully phased-in basis.

The Proposal also provides for an ACL adjustment to Tier 2 capital, which is similar to an existing adjustment to Tier 2 capital for allowance for loan and lease losses. Tier 2 capital relief is not sufficient due to the significantly higher cost of common equity. Binding constraints for the majority of banks' minimum capital levels are CET1 and Tier 1 capital; CET1 will absorb the changes to provision expense from implementing CECL. As such, the capital rule should be modified to address the direct impact of CECL on CET1 in order for any change to the capital rule to have a meaningful impact on banks' capital allocation.

The Agencies have not objected, to any significant degree, to capital plans submitted by financial institutions since 2013. As a result, it appears reasonable to conclude that further increases to capital levels are not warranted, and that permanent adjustments to the regulatory framework must be adopted in connection with the implementation of CECL. BB&T recommends the Agencies consider modifications to the capital rule to achieve capital neutrality that give appropriate consideration to the differences between incurred and expected losses. BB&T recommends the Agencies amend the capital rules to adjust CET1 for CECL reserves that exceed a fixed time horizon (e.g., one year) or adjust risk-weighted assets so a comparable outcome is achieved. Alternatively, the Agencies could decrease minimum capital requirements to reflect CECL's reduction in banks' CET1 unrelated to changes in a banks' risk profile.

#### **Incorporation of CECL in CCAR Stress Test**

As stated above, the Proposal does not address the impact of CECL on minimum capital requirements. Under another proposal, the Board of Governors of the Federal Reserve System ("Board") is considering the creation of the SCB, which will calibrate minimum capital requirements based on the CCAR stress test results. There is currently no specific stress test guidance on how to calculate ACL post-CECL implementation. The Board should provide simple and realistic industry guidance to ensure uniform implementation of CECL into the CCAR stress test to promote comparability and transparency in the stress test results.

As it relates to the incorporation of CECL into the stress testing process, it is not realistic or operationally feasible to require a full CECL estimate for each quarter in the scenario horizon. At a minimum, this would require 27 discrete economic forecasts (i.e., nine quarters of macro-economic forecasts for each scenario (i.e., baseline, adverse and severely adverse). The full complement of models would have to be run for each of the 27 economic forecasts and either use perfect foresight (because the scenarios are known) front-loading all losses, or ignore knowledge of the future and predict an allowance for each of the nine quarters, which will require subjective assumptions.

The incorporation of CECL into the stress testing process must strike an appropriate balance between operational simplicity, transparency and the avoidance of unintended consequences. This could be achieved by leveraging the current allowance estimation process used by CCAR banks in the stress testing process, adjusted to reflect the implementation of CECL, as more fully described below:

- The CCAR methodology should recognize provision build throughout the stress period, as opposed to full recognition in the first quarter, to align with the actual increase of ACL during severely adverse economic conditions. In doing so, the minimum capital ratios will occur closer to the timing of peak stress (i.e., timing of maximum unemployment rates).
- BB&T believes this could be accomplished by leveraging the output from the existing stress test credit models, which are expected loss models, to estimate ACL under CECL. Most banks are using their CCAR models with modest modification (such as taking out new volume assumptions) for CECL.
  - CCAR models create forecasts of future losses consistent with a given stress scenario.
  - In each quarter of the stress test, the stressed ACL should equal the future four quarters net charge-offs plus an adjustment for factoring in life-of-loan credit losses occurring outside the four-quarter horizon. The adjustment could use a simple methodology, such as applying a coverage ratio multiplier or the long-term average expected loss for the remaining life of the portfolio.
  - CECL reflects an allowance estimate on static pools at the balance sheet date and CCAR stresses the beginning balance sheet. The primary issue for CECL in stress testing is new loan originations over the nine-quarter horizon. The current expected loss CCAR models account for new loan originations, which addresses this issue.
- Executing CECL estimates quarterly by applying the full CECL regime used for GAAP as the stress scenarios unfold within CCAR will be unwieldy and does not provide incremental value to CCAR's principal objective of capital stress testing.
- Requiring the ending reserve to cover a specified period of losses past the nine quarters, or an estimate of losses based on long-term expected loss rates, eliminates the challenge of knowing a different baseline forecast in each of the nine quarters and maintains consistency and integrity in the process.

#### **Timing of CECL Incorporation into the CCAR stress test**

The Proposal delays the implementation of CECL into CCAR until after the 2019 stress test cycle. BB&T recommends modifying the proposed deferral to require the incorporation of CECL into CCAR in the stress testing year following adoption of CECL. Factors that BB&T considered relevant in making this recommendation include the following:

- CECL introduces new processes, assumptions, and limitations, which could result in instability in the stress test results and SCB.
- To the extent that the implementation of CECL is not delayed, most banks likely will be adopting the CECL framework on January 1, 2020. However, they will not report on the actual results for the first time until mid-April 2020 at the earliest.

- CCAR submissions are typically due on April 5<sup>th</sup> of each year. As such, the results of the 2020 stress test cycle will be submitted before the first required CECL public disclosures related to the first quarter of 2020.
- There is significant operational complexity and uncertainty involved in implementing CECL into accounting methodology and CCAR reporting concurrently in the first quarter of 2020. This will potentially create both operational and governance challenges at the participating institutions.
- Both CCAR and CECL use expected loss models, hence no real change is needed for CCAR to account for CECL, particularly if CECL is incorporated into CCAR using the above recommended incorporation of CECL into the CCAR stress test.
- Delaying the implementation of CECL in capital planning/stress testing exercises until the year following CECL implementation will allow both banks and the Board to become accustomed to revised processes relative to the execution of CECL.

### **Conclusion**

In closing, BB&T recommends the Agencies consider the above suggestions regarding the implementation of CECL into the Capital Rules. BB&T appreciates the opportunity to provide its comments to the Agencies.

Sincerely,



Daryl N. Bible  
Chief Financial Officer